Senate Standing Committee on Economics

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Additional Estimates

13 – 14 February 2013

Question: AET 76-80

Topic: Mining Industry

Written: Received from Committee – 22 February 2013

Senator BUSHBY asked:

76. At Supplementary Budget Estimates in October 2012, Dr. Gruen stated that the economy has seen the impact of significant falls in the price of commodities such as iron ore, thermal coal and coking coal (Hansard, Thursday 18 October 2012, p. 46). Since then, there has been a dramatic rise in the price of iron ore and both thermal and coking coal.

    How do current spot prices compare with those at the time of the Budget?

77. At Supplementary Budget Estimates in October 2012, Dr. Gruen described the resource boom as a multifaceted phenomenon that should be thought of in three phases (Hansard, Thursday 18 October 2012, p. 47). Dr. Gruen also said at that time that the price boom is over.

    Can Treasury outline how recent rises in commodity prices since October 2012 fit into Dr. Gruen's three-phase boom discussed at Estimates in October?

78. At Supplementary Budget Estimates in October 2012, Dr. Gruen stated in the context of the investment boom that supply will meet demand at a price.

    a. Did Treasury not anticipate the fall in commodity prices between Budget 2012 and October 2012?

    b. Did these price falls arise as a result of additional supply coming on? Was that additional supply detected by Treasury?

    c. If these price falls did not arise solely as a result of additional supply, was it a result of other factors leading to a short-term fall in price which has now rebounded? If this is the case, what factors led to the drop in price?

79. At Supplementary Budget Estimates in October 2012, Dr. Gruen stated that Treasury was expecting a 45 per cent increase in mining investment this financial year (Hansard, Thursday 18 October 2012, p. 70).

    a. Can Treasury provide an update on that figure?

    b. Are the recent increases in commodity prices likely to drive further investment?

    c. Does that change Treasury's assessment of when the investment boom will peak?

80. At the Supplementary Budget Estimates in October 2012, Mr Duggan indicated that in his conversations with mining companies, the cost of doing business and increased union activity on mining sites had not been raised with him at that time.

a. Have the above issues been raised with anyone at Treasury either before October 2012 or since, specifically in the context of cost controls becoming increasingly more important for mining investment?

b. What mining costs does Treasury consider to be within the realm of Government decision makers to reasonably influence?

Answers:

76. The iron ore spot price at the time of the release of the 2012-13 Budget was $US143 per tonne (FOB). The current iron ore spot price (14 Mar 2013) is $US133 per tonne.

The thermal coal spot price at the time of the release of the 2012-13 Budget was $US98 per tonne (FOB). The current thermal coal spot price (8 Mar 2013) is $US92 per tonne.

The current metallurgical coal spot price (14 Mar 2013) is lower than it was at the time of the release of the 2012-13 Budget. Metallurgical coal prices are provided by a commercial vendor.

77. At Supplementary Budget Estimates in October 2012, Dr. Gruen stated that it is helpful to think of the resources boom in Australia as having three phases.

The first phase, which lasted quite a long time, was a period in which demand continued to grow more strongly than most forecasters, including mining companies, had expected. During that first phase, supply of resources took a long time to be able to be ramped up. Over that period, which lasted from late-2003 to something like the second half of last year with the important interruption of the global financial crisis which after all was more than just a parenthesis, we saw very large rises in prices. The first phase saw very large rises in prices for Australia's main resource exports.

Prices for iron ore, thermal coal and metallurgical coal remain well below their levels in the second half of 2011. The period of very large rises in prices for Australia’s main resource exports therefore appears to have ended in the second half of 2011.

78.

a. In the 2012-13 Budget Treasury forecast a decline in the terms of trade of 5¾ per cent for 2012-13. The fall in commodity prices between the 2012-13 Budget and October was larger than was anticipated by the Treasury.

b. Market prices for bulk commodities are determined by the interaction between global demand and supply. While the Bureau of Resources and Energy Economics forecast a modest increase in the global supply of bulk commodities in 2012, it is unlikely that this was the main driver of the significant reduction in prices that was observed. The subsequent increase in prices since December 2012 suggests that the main driver of the decrease and subsequent increase in bulk commodity prices were changes in global demand.

c. In the 2012-13 MYEFO Treasury outlined a number of factors influencing bulk commodity prices. For thermal coal this included subued global demand for coal use in electricity generation, including in response to low gas prices in the United States, and greater global coal supplies becoming available in the Asian market.

Iron ore and metallurgical coal are the main inputs to steel production and the price falls largely reflected weaker demand for steel, consistent with subdued conditions in the major advanced economies and moderation of steel demand growth in the emerging market economies of Asia. Lower steel prices in China also reflected overcapacity in the Chinese steel industry, which added to the seasonal destocking of iron ore and coal that takes place in the third quarter.

79.

a. The most recent ABS survey shows that resources companies expect to increase their capital expenditure by 28 per cent this financial year.

b. Resource investment decisions are taken over a longer-term horizon and are underpinned by projections of global resource needs. Short-term price movements are unlikely to have a significant impact on investment decisions but sustained movements will. The MYEFO forecasts are based on an expectation of commodity prices, aside from cyclical volatility, falling gradually over the medium term as the increased global supply steadily comes online.

c. Resources investment is expected to peak over the next year or so, although it is expected to remain at an historically high level through to the middle of the decade. The exact timing of the peak is inherently difficult to predict, and will depend on, amongst other things, the timing of capital expenditure on major projects currently under construction and the outcome of decisions regarding uncommitted projects.

80.

a. Since the commodity price falls seen in the middle of 2012, cost-cutting has been a key theme in discussions with resources companies. These discussions continue to suggest that the appreciation of the Australian dollar has been a key factor behind the increase in their costs over this time.

Another key factor raised is that the record volume of projects currently under construction, both in Australia and overseas, has resulted in strong demand for labour and capital, bidding up the prices of wages and other specialist inputs.

b. The major drivers of cost growth are determined by the market and are largely outside the influence of government decision makers. However, as is the case for other industries, fiscal (including taxes and subsidies) and regulatory settings, both federal and state, can have an influence on the cost of doing business.